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STATUTES.

IN THE

SUPREME COURT

OF THE

UNITED STATES.

October Term, 1937.

No. 772

LINDSAY-STRATHMORE IRRIGATION DISTRICT,

Appellant,

vs.

MILO W. BEKINS and REED J. BEKINS, as Trustees appointed by the Will of Martin Bekins, Deceased, *et al.*,

Appellees.

BRIEF OF APPELLANT.

I.

Opinion of the Court Below.

The opinion of the District Court of the United States for the Southern District of California, from the judgment of which court this appeal is taken, is found in 21 Fed. Supp., at page 129.

II.

Jurisdiction.

Probable jurisdiction of this court has already been noted and motion to dismiss or affirm for lack of jurisdiction has been denied.

III.

Statement of the Case.

Appellant, Lindsay-Strathmore Irrigation District, is an irrigation district organized on October 25, 1915, under the Statute of California known as the "Irrigation District Act" (approved March 31, 1897), Stats. Calif. 1897, p. 254, Deering Gen. Laws, Act 3854, and acts amendatory thereof and supplemental thereto.

It comprises approximately 15,260 acres located in Tulare County, California.

It is a taxing agency organized and created for the purpose of constructing, maintaining and operating projects and works devoted to the improvement of the lands within its boundaries for agricultural purposes, by making provision for the distribution of water for irrigation and domestic purposes.

It is insolvent and unable to meet its debts as they mature. It has prepared a plan for the composition of its debts, which plan it seeks to have confirmed.

Its indebtedness consists of the outstanding bonds of its two issues of bonds and the accumulated interest thereon. The two issues are designated "first issue" and "second issue" and both issues are 6% semi-annual coupon bonds maturing serially. The first issue is dated July 1, 1916, and was originally issued for $1,400,000.00 of principal, of which issue bonds aggregating $1,192,000.00 of principal remain outstanding. The second issue is dated October 1, 1918 and was originally issued for $250,000.00 of principal of which second issue bonds aggregating $235,000.00 of principal remain outstanding. In addition to the outstanding principal of the bonds, coupons

which have matured since the default of the district, which occurred on July 1, 1933, are unpaid, and, in addition to the coupon interest, further interest at 7%, as is provided for in section 52 of the Irrigation District Act, has accumulated on matured bonds and coupons presented but not paid. The total of such additional indebtedness, representing the matured and unpaid coupons and the further interest at 7%, calculated as of October 1, 1937, is approximately $439,085.15, and the total matured indebtedness of the District for principal and interest upon its said bonds as of the date of the filing of its petition was the sum of $756,085.15. Upon the assessment levied in the year 1932, there was a delinquency of 47% and since said year, the District, pursuant to the provisions of a statute of the state, has levied only an assessment of sufficient amount to maintain and operate the works of the district.

The plan of the district for the composition of its debts is in its central and general feature, one which provides for the payment in cash of a sum equal to 59.978 cents for each dollar of the principal amount of each outstanding bond. This payment is offered to the creditor bondholders in satisfaction of all amounts of principal and interest payable under the terms of the bonds or by reason of presentation as is provided in section 52 of the Irrigation District Act.

Creditors owning approximately 87% in the principal amount of the outstanding bonds, have in writing accepted the plan and consented to the filing of the petition by which the District seeks the confirmation of its plan of composition.

On September 21, 1937, the District sought to have its plan confirmed under the provisions of Chapter X (Sec-

tions 81, 82, 83 and 84) of the Bankruptcy Act (See Appendix A) by filing its verified petition in the District Court of the United States for the Southern District of California. The petition *[R. 1.....] contained allegations substantially as above recited and otherwise complied with the provisions of that Chapter. On the same day the court made and entered its order [R. 15.....] approving the petition as properly filed, fixed a time and place for hearing and directed notice to the creditors. Such notice was duly given. [R. 59-301-64 A 18

On September 22, 1937, the court made a further order [R. 19.....] directing the creditors to show cause why an injunction should not issue staying, pending the determination of the matter, the commencement or continuation of suits on account of the securities affected by the plan, and fixing a time for hearing thereon and directing notice thereof. Such notice was duly given. [R. 61.....]

Certain creditors of the District, Milo W. Bekins and Reed J. Bekins, as Trustees appointed by the Will of Martin Bekins, deceased, and by the Will of Katherine Bekins, deceased, J. R. Mason, James Irvine, A. Heber Winder, Trustee for Eva A. Parrington Trust, C. A. Moss and James H. Jordan, who are appellees here and who hold some of the outstanding bonds of the District, seasonably appeared and made return to the order to show cause [R. 25.....] and also moved to dismiss [R. 21.....] the petition and proceedings on the ground that the court

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*Due to the fact that the printed record has not been received by counsel and cannot be received in time to permit the filing of this brief twenty-one days before the case is called for hearing, as required by the rules of this court, it is impossible to refer to the record. Permission to insert the page references after the brief is filed is requested.

was without jurisdiction and the act under which the proceeding was brought was unconstitutional and void for the following reasons:

1. That the act is not a uniform law on the subject of bankruptcy throughout the United States.

2. That under the act private property may be taken for public use without just compensation contrary to the provisions of the Fifth Amendment.

3. That said act is an attempt to subject state governmental agencies to the jurisdiction of federal courts contrary to the plan and scheme of government as set out in the Constitution of the United States.

The constitutionality of an act of Congress being thus drawn in question, the judge, pursuant to the provisions of the Judiciary Reform Act (50 Stats. 75, U. S. C. A. Title 28, Sec. 401. See Appendix B) duly certified [R. 65.] that fact to the Attorney General of the United States and allowed the government to intervene and the government did so intervene. [R. 68.]

Thereafter, and on November 13, 1937, the court dismissed [R. 69.] the petition and proceeding upon the ground that Chapter X is unconstitutional in that it is subject to the same constitutional infirmities which inhered in Chapter IX of the Bankruptcy Act and as was determined by this court in its decision in the case of *Ashton v. Cameron County Water Improvement District No. 1* (298 U. S. 513, 56 Sup. Ct. Rep. 892).

This appeal from that judgment of dismissal is taken under and pursuant to section 1 of the Act of August 24, 1937, C. 754; 50 Stat. 75, 752; U. S. C. A. Title 28, section 349a. (See Appendix C.)

The lower court filed an opinion [R. 77...] from which it clearly appears that the judgment of dismissal followed the determination of the court that Chapter X is unconstitutional for the same reasons assigned in the *Ashton* case for holding Chapter IX unconstitutional. The other constitutional objections to Chapter X set forth in the motion to dismiss are therefore only briefly considered.

IV.

Specifications of Error Intended To Be Urged.

The assigned errors intended to be urged upon this appeal are:

1. The lower court erred in holding that the Act of Congress (Chapter X of the Bankruptcy Act—August 16, 1937, C. 657, 50 Stats, 659, U. S. C. A. Title X7, sections 401-404) is unconstitutional as applied to the petition of the petitioner, Lindsay-Strathmore Irrigation District.

2. The lower court erred in dismissing the petition of Lindsay-Strathmore Irrigaiton District and the proceedings brought under the above mentioned Act of Congress upon the ground that the act under which the petition was filed is unconstitutional.

3. The lower court erred in vacating and setting aside the order to show cause why a restraining order should not issue and the plan of composition be made temporarily operative.

ARGUMENT.

V.

Summary of Argument.

I. The Statute—Chapter X of the Bankruptcy Act—is a uniform law "on the subject of bankruptcies" and within the express power vested in Congress.

II. Chapter X is not a violation of the Fifth Amendment of the Federal Constitution.

III. Chapter X as applied to the appellant herein and to the plan of composition proposed is not an unconstitutional exercise of the bankruptcy power and does not encroach upon, interfere with, or seek to control the sovereign powers of the state in that

(a) Chapter X is a "composition" act and its operation as such an act cannot result in any interference with the sovereignty of the states.

(b) Chapter X is separable in its provisions and its applications. The appellant district is of such a nature and its plan of such a character that no encroachment upon or interference with the sovereignty of the state can result from its application in this case.

POINT I.

The Statute—Chapter X of the Bankruptcy Act—Is a Uniform Law "on the Subject of Bankruptcies" and Within the Express Power Vested in Congress.

The motion to dismiss [R. 22] assigned as one of the grounds upon which it was based that the Act—Chapter X—was not within the powers of Congress for the reason that it was not a uniform law on the subject of bankruptcy. The lower court did not specifically pass on this objection. The decision in the *Ashton* case assumes Chapter IX to "be adequately related 'to the subject of bankruptcies'" and the cases therein cited seem a conclusive answer to this contention with respect to Chapter X.

Hanover Nat. Bank v. Moyses, 186 U. S. 181, 46 L. Ed. 1113;

Continental Illinois Nat. Bank & Trust Co. v. Chicago R. I. & P. R. Co., 294 U. S. 648, 79 L. Ed. 1110;

Louisville Joint Stock Land Bank v. Radford, 295 U. S. 555, 79 L. Ed. 1593;

Kunzler v. Kohans, 5 Hill 317;

In re Rieman, 7 Ben. 455, Fed. Cas. No. 11673.

POINT II.

Chapter X Does Not Violate the Provisions of Fifth Amendment.

Congress has power to pass legislation pertinent to any of the powers conferred by the Constitution however it may operate collaterally or incidentally to impair or destroy the obligation of private contracts. Under the bankruptcy power the legislation is valid though drawn with the direct intent and purpose of relieving insolvent debtors from the payment of their obligations.

Hanover Nat. Bank v. Moyses, supra;

Continental Ill. Nat. Bank & Tr. Co. v. Chicago R. I. & P. R. Co., supra.

POINT III.

Chapter X As Applied to the Appellant Herein, and to the Plan of Composition Proposed, Is Not An Unconstitutional Exercise of the Bankruptcy Power and Does Not Encroach Upon, Interfere With or Seek To Control the Sovereign Powers of the State.

A. Chapter X is a "Composition" Act and its Operation as Such an Act Cannot Result in Any Interference With the Sovereignty of the States.

Chapter X was enacted by the Congress with the constitutional infirmities of its previously enacted Chapter IX clearly before it. The same social or economic problems were sought to be solved by both enactments. [See "Report by Committee on the Judiciary on H. R. 5969," Appendix "D".) The very limited and restricted nature of the remedy available under the bankruptcy power and of choice in procedural machinery, naturally results in much similarity in the two enactments. These considerations, therefore, combine to emphasize the importance and significance of such differences as appear in the two enactments.

> *Wright v. Vinton Branch of the Mountain Bank* (1937), 300 U. S. 440 at 461, 463, 81 L. Ed. 736.

One such difference is that Chapter X nowhere authorizes the confirmation of a plan of "readjustment". Nor does it speak of, allude or refer to a plan of "readjust-

ment" being effectuated under its provisions. Compared with the previously enacted Chapter IX it substitutes a plan of "composition" for the plan of "readjustment". It is only in Section 83(b) that any word implying an "adjustment" is used in reference to the operation of the enactment. There the language used is "the payment . . . shall be . . . postponed or extended or otherwise *readjusted* in the same manner . . . as if such plan had been finally confirmed." In every instance throughout the entire enactment the "plan" is consistently and always called or referred to as a plan of "composition". With reference and in allusion to the prior enactment, in Section 83(h), Chapter X refers to it as a statute relating to the "refinancing or readjustment of indebtedness of municipalities, political subdivisions, or districts." The Congress carefully avoided any allusion to any prior or existing statute relating to the "composition" of such indebtedness.

In the light of the long line of decisions dealing with compositions, and from which an exposition of their nature can be ascertained, the expression of legislative intent is one of more settled and definite meaning.

The central and basic idea of a composition is that it is voluntary and not coercive. It is an agreement. It originates in a voluntary offer by the debtor and results, in the main, from voluntary acceptance by the creditors.

Naussau Smelting & Refining Works, Ltd., v. Brightwood Bronze Foundry Company (1924), 265 U. S. 269 at 271, 68 L. Ed. 1013.

In some respects it supersedes and is outside of bankruptcy and the respective rights of the debtor and creditors are fixed by their bargain.

In re Lane (1903), 125 Fed. 772 at 773;

In re Landquist et al. (1934), 70 Fed. (2d) 929 at 933;

Myers v. International Trust Company (1927), 273 U. S. 380 at 383, 71 L. Ed. 692;

Cumberland Glass Mfg. Co. v. De Witt (1915), 237 U. S. 447 at 453, 454, 59 L. Ed. 1042.

It is not analogous to an "adjustment".

Louisville Joint Stock Land Bank v. Radford (1935), 295 U. S. 555 at 586, 79 L. Ed. 1593.

No compulsion is brought to bear upon the debtor in a composition case. The composition must originate in the voluntary offer of the debtor. Coercion is felt only by the dissenting minority of creditors when the plan is confirmed.

In confirming a composition the bankruptcy court does not interfere with any fiscal or financial matter or policy of the state or of the debtor agency. Those matters and policies are all previously determined outside of the bankruptcy court.

This is emphasized by another difference in the two enactments. Chapter IX, Section 80(f), provides that the plan and "order of confirmation shall be binding upon (1) the taxing district, and (2) all creditors, etc." Chapter X in its corresponding provisions, Section 83(f) omits the provision making the order or decree binding upon the taxing district. The district is bound by its composition

agreement. No other binding force is necessary or provided for.

It is only in a denial of confirmation upon the ground that the composition is unfair, or that it is not equitable, or that it is not for the best interests of the creditors, or that it is discriminatory, or perhaps, on some other of the grounds enumerated in the enactment (Section 83(e)), that the bankruptcy court by its act may be said to touch upon any fiscal or financial matter or policy of the state or of the debtor agency. So denying and thereby declining to interfere could not be called an act of interference.

The plan of composition of this appellant is a composition in its most simple and elemental form. It provides for the payment in cash of a stated percentage of the indebtedness in exchange for a release from the debt. It was prepared and perfected outside of the bankruptcy court and before the intervention of the bankruptcy court was sought. The rights of the many creditors who have accepted the plan are already fixed by their bargain. The dissenting appellees will, if the plan is confirmed, have their rights in the same measure and as fixed by the terms of the same proposal and not by any term or provision inserted therein or taken therefrom by any act of the court. No modifications or changes in the plan have been made. Needless to say, none are contemplated. No change or modification could be made without the written acceptance of the District (Sec. 83(e)). The terms of the plan or proposal are, in any event, as fixed by the agreement of the District. In the case here, therefore, it could not be said that the federal government by any act on its part interferes with any fiscal, financial or

other policy of the District or with any attribute of sovereignty it may be said to possess or with the sovereignty of the state. As applied to the case here, Chapter X is free of the constitutional infirmities of Chapter IX.

The Abby Dodge v. United States (1912), 223 U. S. 166 at 175, 56 L. Ed. 390 at 393;

Liverpool, N. Y. and P. Steamship Company v. Commissioners, etc. (1885), 113 U. S. 33 at 39, 28 L. Ed. 899;

Yazoo & Mississippi Valley R. R. Co. v. Jackson Vinegar Company (1912), 226 U. S. 217 at 219, 57 L. Ed. 193.

B. CHAPTER X IS SEPARABLE IN ITS PROVISIONS AND APPLICATIONS. THE APPELLANT DISTRICT IS OF SUCH NATURE AND ITS PLAN OF SUCH CHARACTER THAT NO ENCROACHMENT UPON OR INTERFERENCE WITH THE SOVEREIGNTY OF THE STATE CAN RESULT FROM ITS APPLICATION.

Another important difference which appears upon comparison of the two enactments lies in the fact that Chapter IX by its terms was limited in its application to political subdivisions.

Re Imperial Irrigation District (1936), 87 Fed. (2d) 355,

whereas Chapter X by its terms applies to the six separably enumerated kinds or classes of taxing agencies.

It might well be said that, in limiting the application of Chapter IX to "political" subdivisions, the Congress made it impossible for the courts to separably apply its

provisions to a subdivision not possessed of any significant attribute of sovereignty.

Yu Cong Eng v. Trinidad (1926), 271 U. S. 500 at 518; 70 L. Ed. 1059,

particularly in view of the many previous decisions in nearly every court in the land which, in tax cases, eminent domain cases, tort cases, execution upon property cases, and no doubt other kinds of cases, turned upon the distinctions implicit in such words as "political," "public," "governmental" and the like, on the one hand and such words as "private," "corporate," proprietary" and the like, on the other hand. In such view the water district in the *Ashton* case was before the court in its character as a "political" subdivision necessarily exercising governmental functions, else it was not properly before the court at all. Any attempt to separably apply the provisions of Chapter IX to a subdivision which is non-political or to a non-political enterprise of a subdivision could only present a moot question.

In Chapter X the case is different. It contains an expression, in the clearest terms of which language is capable, of the legislative intent that it be a statute separable in its provisions and in its applications (Sec. 81).

Trade Mark Cases (1879), 100 U. S. 82 at 98; 25 L. Ed. 550, 553;

The Abby Dodge v. United States (1912), 223 U. S. 166 at 175; 56 L. Ed. 390;

Dorchy v. Kansas (1924), 264 U. S. 286 at 290; 68 L. Ed. 686;

National Labor Relations Board v. Jones & Laughlin Steel Corporation (1937), 301 U. S. 1 at 29; 81 L. Ed. 893.

Obviously none of the constitutional consequences of encroachment upon or interference with the sovereignty of the states in the exercise of a power expressly conferred, can follow except there be an interference with or encroachment upon the sovereignty or some of its essential attributes. In the separable application of Chapter X in the instant case therefore, he who would invoke such a constitutional consequence should first clearly show the attribute of sovereignty being actually and appreciably encroached upon or interfered with in the constitutional sense.

Metcalf v. Mitchell (1926), 269 U. S. 514 at 524; 70 L. Ed. 384;

Willcuts v. Bunn (1931), 282 U. S. 216 at 234; 75 L. Ed. 304 at 312;

Trustees of the University of Illinois v. United States (1933), 289 U. S. 48 at 59; 77 L. Ed. 1025 at 1029;

Helvering v. Powers (1934), 293 U. S. 214 at 224; 79 L. Ed. 291;

Ohio v. Helvering (1934), 292 U. S. 360 at 369; 78 L. Ed. 1307.

This means a showing either (1) that the appellant district is of such a character and is so intimately connected with the sovereignty of the state in the exercise of the essentially governmental functions of the state that it cannot be touched by the federal government in the exercise of an express power, without thereby interfering with the state in its exercise of an essentially governmental function or (2) a showing that a burden, or an inter-

ference, or an encroachment, which is real, not imaginary, substantial and not negligible, results from the mere confirmation of the plan of this district for the composition of its previously existing indebtedness.

The appellant district is a local organization to secure a local benefit to be derived from the irrigation of lands from the same source of water supply and by the same system of works, and from which the state, or the public at large, derives no direct benefit, but only that reflex benefit which all local improvements confer.

> *City of San Diego v. Linda Vista Irrigation District, et al.* (1895). 108 Cal. 189 at 193.

If it possesses any governmental powers at all it possesses only those appropriate for that single purpose.

> *In re Madera Irrigation District* (1891), 92 Cal. 296 at 318.

Jenison v. Redfield, 149 Cal. 503

Any contention that it is inextricably connected with the sovereignty of the State of California finds no support in the decisions of the highest court of that state which would not result from the admitted impossibility (or undesirability) of formulating a rule by which the "political," "public" or "governmental" activities or functions of an agency are to be distinguished from its "private," "corporate" or "proprietary" activities or functions, in tort cases, eminent domain cases, execution upon property cases, and tax cases. In cases where the court has been more or less free from this confusion of precedent, the real nature and character of the district is more clearly revealed. Although such districts are by state law clothed with the usual immunity from tort liability and from

taxation and possess the right of condemnation, it was held in

Crawford v. Imperial Irrig. Dist. (1927), 200 Cal. 318

that an irrigation district is not a municipal corporation within the meaning of the rule of law prohibiting the expenditure of public funds unless authorized by statute, and in

Wood v. Imperial Irrig. District (1932), 216 Cal. 748

it was held that a provision in the State Bank Act permitting a bank to secure the deposits of cities, towns * * * "and any other governmental or political subdivision" did not authorize a bank to secure the deposits of an irrigation district. With further reference to the status of an irrigation district as a "political subdivision" the California District Court of Appeal in

Huck v. Rathjen (1924), 66 Cal. App. 84

which involved the contest of an election of a director of an irrigation district brought under a statute authorizing such proceeding by any elector of "any political subdivision of either" (city or county) and presenting the single question whether or not an irrigation district was a political subdivision of a county, plainly said (page 85) that an irrigation district is "not a political subdivision at all." It was also held by the Supreme Court of California in

Bettencourt v. Industrial Accident Comm. (1917), 175 Cal. 559

that reclamation districts, organized under a statute very similar to the statute under which the appellant district

is organized "possess no political or governmental powers, are not organized for political or governmental purposes and are therefore not public corporations at all."

It would therefore seem clear that the separable application of the provisions of Chapter X to the plan of composition of this appellant district cannot result in any interference with or encroachment upon the sovereignty of the state or of the district.

For the above reasons the judgment of the court below dismissing the petition and vacating the order to show cause should be reversed and the case remanded for further proceedings.

Respectfully submitted,

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A copy of this brief has been served on opposing counsel.

JAS. R. MCBRIDE,
Counsel for Appellant.

APPENDIX "A".

"An act to amend an Act entitled 'An Act to establish a uniform system of bankruptcy throughout the United States', approved July 1, 1898, and Acts amendatory thereof and supplementary thereto.

"Be It Enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Act of July 1, 1898, entitled 'An Act to establish a uniform system of bankruptcy throughout the United States', as approved July 1, 1898, and Acts amendatory thereof and supplementary thereto be, and they are hereby, amended by adding thereto a new chapter, to be designated 'chapter X', to be and read as follows:

'Chapter X

'Additional Jurisdiction

'Sec. 81. This Act and proceedings thereunder are found and declared to be within the subject of bankruptcies and, in addition to the jurisdiction otherwise exercised, courts of bankruptcy shall exercise original jurisdiction as provided in this chapter for the composition of indebtedness of, or authorized by, any of the taxing agencies or instrumentalities hereinafter named, payable (a) out of assessments or taxes, or both, levied against and constituting liens upon property in any of said taxing agencies or instrumentalities, or (b) out of property acquired by foreclosure of any such assessments or taxes or both, or (c) out of income derived by such taxing agencies or instrumentalities from the sale of water or power or both, or (d) from any combination

thereof; (1) Drainage, drainage and levee, levee, levee and drainage, reclamation, water, irrigation, or other similar districts, commonly designated as agricultural improvement districts or local improvement districts, organized or created for the purpose of constructing, improving, maintaining, and operating certain improvements or projects devoted chiefly to the improvement of lands therein for agricultural purposes; or (2) local improvement districts such as sewer, paving, sanitary, or other similar districts, organized or created for the purposes designated by their respective names; or (3) local improvement districts such as road, highway, or other similar districts, organized or created for the purpose of grading, paving, or otherwise improving public streets, roads, or highways; or (4) public-school or public-school authorities organized or created for the purpose of constructing, maintaining, and operating public schools or public-school facilities; or (5) local improvement districts such as port, navigation, or other similar districts, organized or created for the purpose of constructing, improving, maintaining, and operating ports and port facilities; or (6) any city, town, village, borough, township, or other municipality: *Provided, however,* that if any provision of this chapter, or the application thereof to any such taxing agency or district or class thereof or to any circumstance, is held invalid, the remainder of the chapter, or the application of such provision to any other or different taxing agency or district or class thereof or to any other or different circumstances, shall not be affected by such holding.

'Definition

'Sec. 82. The following terms as used in this chapter, unless a different meaning is plainly required by the context, shall be construed as follows:

'That the term "petitioner" shall include any taxing agency or instrumentality referred to in section 81 of this chapter.

'The term "security" shall include bonds, notes, judgments, claims, and demands, liquidated or unliquidated, and other evidences of indebtedness, either secured or unsecured, and certificates of beneficial interest in property.

'The term "creditor" means the holder of a security or securities.

'Any agency of the United States holding securities acquired pursuant to contract with any petitioner under this chapter shall be deemed a creditor in the amount of the full face value thereof.

'The term "security affected by the plan" means a security as to which the rights of its holder are proposed to be adjusted or modified materially by the consummation of a composition agreement.

'The singular number includes the plural and the masculine gender the feminine.

'Compositions

'Sec. 83. (a) Any petitioner may file a petition hereunder stating that the petitioner is insolvent or unable to meet its debts as they mature and that it desires to effect a plan for the composition of its debts. The petition shall be filed with the court in whose territorial jurisdiction the petitioner or the major part thereof is located, and, in the case of any unincorporated tax or special-assessment dis-

trict having no officials of its own, the petition may be filed by its governing authority or the board or body having authority to levy taxes or assessments to meet the obligations to be affected by the plan of composition. The petition shall be accompanied by payment to the clerk of a filing fee of $100, which shall be in lieu of the fees required to be collected by the clerk under other applicable chapters of the Uniform Bankruptcy Act of 1898, as amended. The petition shall state that a plan of composition has been prepared, is filed and submitted with the petition, and that creditors of the petitioner owning not less than 51 per centum in amount of the securities affected by the plan (excluding, however, any such securities owned, held, or controlled by the petitioner), have accepted it in writing. There shall be filed with the petition a list of all known creditors of the petitioner, together with their addresses so far as known to petitioner, and description of their respective securities showing separately those who have accepted the plan of composition, together with their separate addresses, the contents of which list shall not constitute admissions by the petitioner in a proceeding under this chapter or otherwise. Upon the filing of such a petition the judge shall enter an order either approving it as properly filed under this chapter, if satisfied that such petition complies with this chapter and has been filed in good faith, or dismissing it, if not so satisfied.

The "plan of composition," within the meaning of this chapter, may include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through issuance of new securities of any character, or otherwise, and may con-

tain such other provisions and agreements not inconsistent with this chapter as the parties may desire.

'No creditor shall be deemed to be affected by any plan of composition unless the same shall affect his interest materially, and in case any controversy shall arise as to whether any creditor or class of creditors shall or shall not be affected, the issue shall be determined by the judge, after hearing, upon notice to the parties interested.

'For all purposes of this chapter any creditor may act in person or by an attorney or a duly authorized agent or committee. Where any committee, organization, group, or individual shall assume to act for or on behalf of creditors, such committee, organization, group, or individual shall first file with the court in which the proceeding is pending a list of the creditors represented by such committee, organization, group, or individual, giving the name and address of each such creditor, together with a statement of the amount, class, and character of the security held by him, and attach thereto copies of the instrument or instruments in writing signed by the owners of the bonds showing their authority, and shall file with the list a copy of the contract or agreement entered into between such committee, organization, group, or individual and the creditors represented by it or them, which contract shall disclose all compensation to be received, directly or indirectly, by such committee, organization, group, or individual, which agreed compensation shall be subject to modification and approval by the court.

'(b) Upon approving the petition as properly filed, or at any time thereafter, the judge shall enter an order fixing a time and place for a hearing on the petition, which shall be held within ninety days from the date of said order, and shall provide in the order that notice shall be

given to creditors of the filing of the petition and its approval as being properly filed, and of the time and place for the hearing. The judge shall prescribe the form of the notice, which shall specify the manner in which claims and interests of creditors shall be filed or evidenced, on or before the date fixed for the hearing. The notice shall be published at least once a week for three successive weeks in at least one newspaper of general circulation published within the jurisdiction of the court, and in such other paper or papers having a general circulation among bond dealers and bondholders as may be designated by the court, and the judge may require that it may be published in such other publication as he may deem proper. The judge shall require that a copy of the notice be mailed, postage prepaid, to each creditor of the petitioner named in the petition at the address of such creditor given in the petition, or, if no address is given in the petition for any creditor and the address of such creditor cannot with reasonable diligence be ascertained, then a copy of the notice shall be mailed, postage prepaid, to such creditor addressed to him as the judge may prescribe. All expense of giving notice as herein provided shall be paid by the petitioner. The notice shall be first published, and the mailing of copies thereof shall be completed at least sixty days before the date fixed for the hearing.

'At any time not less than ten days prior to the time fixed for the hearing, any creditor of the petitioner affected by the plan may file an answer to the petition controverting any of the material allegations therein and setting up any objection he may have to the plan of composition. The judge may continue the hearing from time to time if the percentage of creditors required herein for the confirmation of the plan shall not have accepted

the plan in writing, or if for any reason satisfactory to the judge the hearing is not completed on the date fixed therefor. At the hearing, or a continuance thereof, the judge shall decide the issues presented and unless the material allegations of the petition are sustained, shall dismiss the proceeding. If, however, the material allegations of the petition are sustained, the judge shall classify the creditors according to the nature of their respective claims and interests; *Provided, however,* That the holders of all claims, regardless of the manner in which they are evidenced, which are payable without preference out of funds derived from the same source or sources shall be of one class. The holders of claims for the payment of which specific property or revenues are pledged, or which are otherwise given preference as provided by law, shall accordingly constitute a separate class or classes of creditors.

'At the hearing or a continuance thereof, the judge may refer any matters to a special master for consideration, the taking of testimony, and a report upon special issues, and may allow reasonable compensation for the services performed by such special master, and the actual and necessary expenses incurred in connection with the proceeding, including compensation for the services rendered and expenses incurred in obtaining the deposit of securities and the preparation of the plan, whether such work may have been done by the petitioner or by committees or other representatives of creditors, and may allow reasonable compensation for the attorneys or agents of any of the foregoing, and may apportion the amount so determined among the parties to the proceeding as may be just: *Provided, however,* That no fees, compensation, reimbursement, or other allowances for attorneys, agents, committees, or other

representatives of creditors shall be assessed against the petitioner or paid from any revenues, property, or funds of the petitioner except in the manner and in such sums, if any, as may be provided for in the plan of composition. An appeal may be taken from any order making such determination or award to the United States Circuit Court of Appeals for the circuit in which the proceeding under this chapter is pending, independently of other appeals which may be taken in the proceeding, and such appeal shall be heard summarily.

'On thirty days' notice by any creditor to petition, the judge, if he finds that the proceeding has not been prosecuted with reasonable diligence, or that it is unlikely that the plan will be accepted by said proportion of creditors, may dismiss the proceeding.

'(c) Upon entry of the order fixing the time for the hearing, or at any time thereafter, the judge may upon notice enjoin or stay, pending the determination of the matter, the commencement or continuation of suits against the petitioner, or any officer or inhabitant thereof, on account of the securities affected by the plan, or to enforce any lien or to enforce the levy of taxes or assessments for the payment of obligations under any such securities, or any suit or process to levy upon or enforce against any property acquired by the petitioner through foreclosure of any such tax lien or special assessment lien, except where rights have become vested, and may enter an interlocutory decree providing that the plan shall be temporarily operative with respect to all securities affected thereby and that the payment of the principal or interest, or both, of such securities shall be temporarily postponed or extended or otherwise readjusted in the same manner and upon the same terms as if such plan had been finally

confirmed and put into effect, and upon the entry of such decree the principal or interest, or both, of such securities which have otherwise become due, or which would otherwise become due, shall not be or become due or payable, and the payment of all such securities shall be postponed during the period in which such decree shall remain in force, but shall not, by any order or decree, in the proceeding or otherwise, interfere with (a) any of the political or governmental powers of the petitioner; or (b) any of the property or revenues of the petitioner necessary for essential governmental purposes; or (c) any income-producing property, unless the plan of composition so provides.

'(d) The plan of composition shall not be confirmed until it has been accepted in writing, by or on behalf of creditors holding at least two-thirds of the aggregate amount of claims of all classes affected by such plan and which have been admitted by the petitioner or allowed by the judge, but excluding claims, owned, held, or controlled by the petitioner: *Provided, however,* That it shall not be requisite to the confirmation of the plan that there be such acceptance by any creditor of class of creditors (a) whose claims are not affected by the plan; or (b) if the plan makes provision for the payment of their claims in cash in full; or (c) if provision is made in the plan for the protection of the interests, claims, or lien of such creditors or class of creditors.

'(e) At the conclusion of the hearing, the judge shall make written findings of fact and his conclusions of law thereon, and shall enter an interlocutory decree confirming the plan if satisfied that (1) it is fair, equitable, and for the best interests of the creditors and does not discriminate unfairly in favor of any creditor or class of

creditors; (2) complies with the provisions of this chapter, (3) has been accepted and approved as required by the provisions of subdivision (d) of this section; (4) all amounts to be paid by the petitioner for services or expenses incident to the composition have been fully disclosed and are reasonable; (5) the offer of the plan and its acceptance are in good faith; and (6) the petitioner is authorized by law to take all action necessary to be taken by it to carry out the plan. If not so satisfied, the judge shall enter an order dismissing the proceeding.

'Before a plan is confirmed, changes and modifications may be made therein, with the approval of the judge after hearing upon such notice to creditors as the judge may direct, subject to the right of any creditor who shall previously have accepted the plan to withdraw his acceptance, within a period to be fixed by the judge and after such notice as the judge may direct, if, in the opinion of the judge, the change or modification will be materially adverse to the interest of such creditor, and if any creditor having such right of withdrawal shall not withdraw within such period, he shall be deemed to have accepted the plan as changed or modified: *Provided, however,* That the plan as changed or modified shall comply with all the provisions of this chapter and shall have been accepted in writing by the petitioner. Either party may appeal from the interlocutory decree as in equity cases. In case said interlocutory decree shall prescribe a time within which any action is to be taken, the running of such time shall be suspended in case of an appeal until final determination

thereof. In case said decree is affirmed, the judge may grant such time as he may deem proper for the taking of such action.

'(f) If an interlocutory decree confirming the plan is entered as herein provided, the plan and said decree of confirmation shall become and be binding upon all creditors affected by the plan, if within the time prescribed in the interlocutory decree, or such additional time as the judge may allow, the money, securities, or other consideration to be delivered to the creditors under the terms of the plan shall have been deposited with the court or such disbursing agent as the court may appoint or shall otherwise be made available for the creditors. And thereupon the court shall enter a final decree determining that the petitioner has made available for the creditors affected by the plan the consideration provided for therein and is discharged from all debts and liabilities dealt with in the plan except as provided therein, and that the plan is binding upon all creditors affected by it, whether secured or unsecured, and whether or not their claims have been filed or evidenced, and, if filed or evidenced, whether or not allowed, including creditors who have not, as well as those who have, accepted it.

'(g) A certified copy of the final decree, or of any other decree or order entered by the court or the judge thereof, in a proceeding under this chapter, shall be evidence of the jurisdiction of the court, the regularity of the proceedings, and the fact that the decree or order was made. A certified copy of an order providing for the

transfer of any property dealt with by the plan shall be evidence of the transfer of title accordingly and, if recorded as conveyances are recorded, shall impart the same notice that a deed, if recorded, would impart.

'(h) This chapter shall not be construed as to modify or repeal any prior, existing statute relating to the refinancing or readjustment of indebtedness of municipalities, political subdivisions, or districts: *Provided, however,* That the initiation of proceedings or the filing of a petition under section 80 shall not constitute a bar to the same taxing agency or instrumentality initiating a new proceeding under section 81 thereof.

'(i) Nothing contained in this chapter shall be construed to limit or impair the power of any State to control, by legislation or otherwise, any municipality or any political subdivision of or in such State in the exercise of its political or governmental powers, including expenditures therefor.

'Termination of Jurisdiction

'Sec. 84. Jurisdiction conferred on any court by section 81 shall not be exercised by such court after June 30, 1940, except in respect of any proceeding initiated by filing a petition under section 83 (a) on or prior to June 30, 1940.'

APPENDIX "B".

Section 401:

"§401. Intervention by United States; constitutionality of federal statute.

Whenever the constitutionality of any Act of Congress affecting the public interest is drawn in question in any court of the United States in any suit or proceeding to which the United States, or any agency thereof, or any officer or employee thereof, as such officer or employee, is not a party, the court having jurisdiction of the suit or proceeding shall certify such fact to the Attorney General. In any such case the court shall permit the United States to intervene and become a party for presentation of evidence (if evidence is otherwise receivable in such suit or proceeding) and argument upon the question of the constitutionality of such Act. In any such suit or proceeding the United States shall, subject to the applicable provisions of law, have all the rights of a party and the liabilities of a party as to court costs to the extent necessary for a proper presentation of the facts and law relating to the constitutionality of such Act."

APPENDIX "C".

Section 349a:

"§349a. Direct appeal to Supreme Court; constitutionality of federal statutes; time; precedence.

In any suit or proceeding in any court of the United States to which the United States, or any agency thereof, or any officer or employee thereof, as such officer or employee, is a party, or in which the United States has intervened and become a party, and in which the decision is against the constitutionality of any Act of Congress, an appeal may be taken directly to the Supreme Court of the United States by the United States or any other party to such suit or proceeding upon application therefor or notice thereof within thirty days after the entry of a final or interlocutory judgment, decree, or order; and in the event that any such appeal is taken, any appeal or cross-appeal by any party to the suit or proceeding taken previously, or taken within sixty days after notice of an appeal under this section, shall also be or be treated as taken directly to the Supreme Court of the United States. In the event that an appeal is taken under this section, the record shall be made up and the case docketed in the Supreme Court of the United States within sixty days from the time such appeal is allowed, under such rules as may be prescribed by the proper courts. Appeals under this section shall be heard by the Supreme Court of the United States at the earliest possible time and shall take precedence over all other matters not of a like character. This section shall not be construed to be in derogation of any right of direct appeal to the Supreme Court of the United States under existing provisions of law."

APPENDIX "D".

REPORT BY COMMITTEE ON THE JUDICIARY ON H. R. 5969

(Sec. 4570) Report by the Committee on the Judiciary recommending the passage of H. R. 5969 which deals with the composition, through proceedings in bankruptcy, of the indebtedness of insolvent taxing agencies.

H. R. 5969 was introduced by Mr. Summers of Texas in the House of Representatives on March 29, 1937. The bill proposes to amend the Bankruptcy Act by adding a chapter to be known as chapter X. It provides for the composition, through proceedings in bankruptcy, of the indebtedness of insolvent taxing agencies such as various improvement districts, and certain towns, cities, boroughs, and townships. The bill was immediately referred to the Committee on the Judiciary and on March 31, 1937, Mr. Chandler, from the Committee, submitted a report in which it was stated that the Committee after consideration favored the bill and recommended its passage. The report in full text follows.

This bill is the outgrowth of public hearings by the Subcommittee on Bankruptcy of the Committee on the Judiciary on H. R. 2505, H. R. 2506, and H. R. 5403, dealing with the same subject, namely, the composition, through proceedings in bankruptcy, of the indebtedness of insolvent taxing agencies such as drainage, levee, water, irrigation, sewer, road, school, port, and similar improvement districts, and certain towns, cities, boroughs, and townships.

Compositions are approvable only when the districts or agencies file voluntary proceedings in courts of bankruptcy accompanied by plans approved by 51 per cent of all the creditors of the district or agency, and by evidence

of good faith. Each proceeding is subject to ample notice to creditors, thorough hearings, complete investigations, and appeals from interlocutory and final decrees. The plan of composition cannot be confirmed unless accepted in writing by creditors holding at least 66 2/3 per cent of the aggregate amount of the indebtedness of the petitioning district or taxing agency, and unless the judge is satisfied that the taxing district is authorized by law to carry out the plan, and until a specific finding by the court that the plan of composition is fair, equitable, and for the best interests of the creditors.

The jurisdiction conferred in the bill terminates on June 30, 1940. One of the primary purposes of the measure is to enable, under proper safeguards, the rehabilitation and reorganization of those taxing districts and agencies which were in process of rearranging and refinancing their obligations under chapter 345 of the Public Acts of the Seventy-third Congress, sections 78, 79 and 80 (48 Stat. 798; title 11, U. S. C., secs. 301, 302, and 303, as amended), when the United States Supreme Court declared that act unconstitutional in the case of *Ashton v. Cameron County Water District* (298 U. S. 513) (Sec. 152). However, any insolvent taxing district or agency may apply for composition under the provisions of this bill, and the need for the legislation is clearly shown by the testimony presented at the hearings.

The Committee on the Judiciary is not unmindful of the sweeping character of the holding of the Supreme Court above referred to, and believes that H. R. 5969 is not invalid or contrary to the reasoning of the majority opinion in the 5-to-4 decision. The act which was declared unconstitutional designated the instrumentalities included in its provisions as *political subdivisions* of the

State, and the Supreme Court determined that it was beyond the power reposed in Congress by article I, section 8, clause 4, of the Federal Constitution, "To establish * * * uniform laws on the subject of bankruptcies," to pass an act to interfere with the States in the control of their fiscal affairs.

The bill here recommended for passage expressly avoids any restriction on the powers of the States or their arms of government in the exercise of their sovereign rights and duties. No interference with the fiscal or governmental affairs of a political subdivision is permitted. The taxing agency itself is the only instrumentality which can seek the benefits of the proposed legislation. No involuntary proceedings are allowable, and no control or jurisdiction over that property and those revenues of the petitioning agency necessary for essential governmental purposes is conferred by the bill.

As the statute which was declared unconstitutional was held to be within the subject of bankruptcies and uniform in its application, *a fortiori,* the present bill is adequately related to the general subject to bankruptcies, and does not conflict with the fifth amendment of the Federal Constitution as to due process of law. *Ashton v. Cameron County Water District* (298 U. S. 513); *Continental, etc. Co. v. C. R. I. & P. Ry.* (294 U. S. 648); *Louisville Joint Stock Land Bank v. Radford* (295 U. S. 555).

The constitutional provision authorizing Congress to establish uniform laws on the subject of bankruptcies contains no exceptions. It is only because the bankruptcy power was authorized in the same section of the Constitution which confers the Federal power to lay and collect taxes that the former power is impliedly limited by the judicial construction placed on the latter power for the

purpose of preserving the independence and sovereignty of the States. Granted the limitation of the Federal taxing power, if the pending bill does not and cannot restrict the control of a State agency over its fiscal affairs, the statute would not be invalid. The States themselves are subject to taxation by the Federal Government except as to operations which are essentially governmental in their nature, and "the immunity of the States from Federal taxation is limited to those agencies which are of a governmental character." (*South Carolina v. U. S.* (199 U. S. 437); *Ohio v. Helvering* (292 U. S. 36-60).

In other words, "the implied limitation on the Federal taxing power, springing from the necessity of maintaining our dual system of Government, does not extend beyond" that necessity; and the bankruptcy power is subject to like interpretation, *Board of Trustees of Illinois v. United States* (289 U. S. 48).

In construing the implied limitation on the Federal taxing power, the cases have been determined on their facts, and if there was no actual interference with essential governmental functions of a State or its agencies, the exercise of the taxing power has been sustained. This rule of construction applies with equal force and effect to the power to establish uniform laws on the subject of bankruptcies, and in itself, justifies the passage of the pending bill to meet conditions deserving legislative assistance.

Therefore, the applicability of the pending bill to any taxing district or agency rests on the corporate character

of each petitioner and depends on the actual interference, if any, with its essential governmental functions; and the saving clause in section 81 of the bill is designed to sustain the measure as to others if any one or more of the taxing agencies classified therein should be held to be political subdivisions exercising sovereign powers.

This bill is intended to remove an apparent impasse, and the committee believes that it will be welcomed by debtors and creditors. When a municipality or a taxing district is insolvent, the creditors cannot foreclose their mortgage, or cause public property to be sold and the proceeds distributed. They must look to the exercise of the taxing power over a period of years, or, in cooperation with the debtor district, must grant extensions. This often involves reorganization of part or all of the debt structure, and hinges upon agreement by debtor and creditor, or on the existence of a Federal statute which may force recalcitrant minority creditors into agreement. Otherwise the creditors of a municipality or a taxing district must resort to mandamus proceedings, which have not been adequate remedies. In fact, the trend of recent decisions has been to deny the writ of mandamus wherever sound judicial discretion justifies denial. Hence, creditors have been unable to obtain unjust advantage, but the problem of the municipality or taxing district has remained unsolved. *Christmas v. City of Asbury Park* (78 Fed. (2d,) 1003). For an embarrassed debtor without the remedy afforded by this bill, the only effective recourse is the repeal of its charter by the State legislature, in which

event creditors are generally left without any remedy. *Meriwether v. Garrett* (102 U. S. 472, 501).

There is no hope for relief through statutes enacted by the States, because the Constitution forbids the passing of State laws impairing the obligations of existing contracts. Therefore, relief must come from Congress, if at all. The committee are not prepared to admit that the situation presents a legislative no-man's land. The power to deal with bankruptcies was given by the Constitution to Congress without express limitation, and, at the same time, the States deprived themselves of the power to deal adequately with the conditions which have arisen. Only analogous judicial construction has blocked the way thus far. It is the opinion of the committee that the present bill removes the objections to the unconstitutional statute, and gives a forum to enable those distressed taxing agencies which desire to adjust their obligations and which are capable of reorganization, to meet their creditors under necessary judicial control and guidance and free from coercion, and to affect such adjustment on a plan determined to be mutually advantageous.

Historically the early bankruptcy statutes were of limited duration, and were intended to provide methods whereby insolvent and failing debtors could be relieved of overwhelming burdens and thus be enabled to make a new start under favorable conditions which generally followed periods of great depression. This bill has a 3-year limitation. That is considered ample time to effect necessary compositions. Permanent legislation of this character

would tend to effect adversely the financial problems of taxing agencies, and the committee, while not expecting unfailing foresight by public officials, cherishes the view that public contracts, especially, should be scrupulously performed whenever possible.

As an aid to insolvent taxing districts, Congress has authorized the Reconstruction Finance Corporation to make loans to such instrumentalities within safe limits as to security and duration. Through this channel, districts and agencies eligible for relief under the pending legislation can apply to the Reconstruction Finance Corporation for sufficient funds to compose their debts. Many acceptable applications are now pending, and others will be made if this bill is enacted into law. Many defaults in public obligations can be removed, and the welfare of thousands of citizens can be promoted by the passage of the bill.